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Secretary:

FPA

Financial Planning Association of Australia Limited
ABN 62 054 174 453
Member freecall 1800 337 301
Consumer freecall 1800 626 393
fpa@fpa.asn.au • www.fpa.asn.au

GPO Box 4285
Sydney NSW 2001

Ph: 02 9220 4500
Fax: 02 9220 4580

16 January 2006

Mr Stephen Boyd
Secretary
House of Representatives Standing Committee on Economics, Finance and Public Administration
Parliament House
CANBERRA ACT 2600

Dear Mr Boyd

EMPLOYER ELIGIBLE TERMINATION PAYMENTS (ETPS)

When the Financial Planning Association of Australia (FPA) gave evidence to the Committee on 18 October concerning its inquiry into increasing superannuation savings by people under 40, an argument was made that an Employer Eligible Termination Payment (ETP) rolled into a superannuation fund should not have to be preserved. This issue had not been included in the written submission which FPA made to the Committee on 23 August 2005.

In order for Committee members to understand fully the points behind the FPA position, the FPA has provided the enclosed short supplementary submission on the ETP issue. For any questions regarding this matter, please contact me on
tel: 02 9220 4513 and email: john.anning@fpa.asn.au.

Yours sincerely

John Anning
Manager Policy and Government Relations

New South Wales / ACT

Queensland

South Australia / NT

Tasmania

Victoria

Western Australia
West Perth WA 6872
Ph 08 9486 1788
Fax 08 9486 1799

Supplementary Submission
to
the House of Representatives Standing Committee on Economics, Finance and Public Administration

Inquiry into Improving the Superannuation Savings of People Under the Age 40

The Case for Non-Preservation of Employer Eligible Termination Payments

JANUARY 2006

Prepared by:
Financial Planning Association of Australia Limited

BACKGROUND

Prior to 1 July 2004, when an individual rolled an employer eligible termination payment (ETP) (eg golden handshakes, bona fide redundancy payments and approved early retirement schemes) into their superannuation fund it was classified as an unrestricted non-preserved benefit, as required by the previous Superannuation Industry (Supervision) Regulation (SISR) 6.10(2).

SISR 2004 (No. 4) amended this subregulation so that only employer ETPs received by a superannuation fund before 1 July 2004 can be classified as unrestricted non-preserved benefits. Therefore, all employer ETPs rolled into superannuation from 1 July 2004 are treated as preserved benefits and are subject to normal preservation rules.

This change has entailed a number of disadvantages.

Individuals may be discouraged from rolling over employer ETPs into superannuation to boost retirement savings

An important plank of Australia's retirement income policy is focussed on the encouragement of voluntary savings. Previously, when individuals received an employer ETP, they were encouraged to roll it over into a superannuation fund as they still could access the funds if their circumstances required.

Most employer ETPs are received due to a redundancy. For many people, this is an unexpected event and their future is often uncertain.

As employer ETPs are now automatically preserved when rolled into a superannuation fund, members lose the flexibility to access funds until a condition of release is met. This change in preservation actively discourages individuals, particularly those far from retirement, from rolling an employer ETP into superannuation as their future uncertainty means they cannot risk losing access to the capital. This could disadvantage individuals who may be worse off from a taxation perspective as the tax is higher on a cash-out.

It is also important to note that when employer ETPs were treated as unrestricted non-preserved benefits, many people chose to retain the money in superannuation. Even if the employer ETP only remained within superannuation for a short time, it could still assist in increasing their retirement savings as the investment earnings would be compounding on a larger amount and those earnings would represent preserved components of a member's superannuation benefit.

If the Government is attempting to lessen the aging population problem that Australia faces by boosting retirement savings, policies are needed that encourage individuals to inject more funds into their superannuation. Preserving employer ETPs that are rolled into superannuation does not do this. Preservation, in this case, acts as a disincentive because people are wary of losing access to funds they may need to draw upon. The chances are though that in most cases, the money is not needed but it is lost to superannuation. FPA understands anecdotally from members that the number of employer ETPs rolled over into superannuation has declined significantly.

The decision to rollover an employer ETP can not be undone
When an employee receives an employer ETP, they have a choice to either receive it directly as cash or to roll it over into a superannuation fund. Whilst many individuals realise the complexity of the issue and seek financial advice, others attempt to make the decision themselves. Often, the employee may have a short time to research the implications of receiving an employer ETP and coupled with the complexity, may make an inappropriate decision.

Previously, if an employee made an inappropriate decision and rolled an employer ETP into superannuation, they could still access the funds. Now, due to the changes in preservation, if an individual makes such a mistake, they do not have the same flexibility which can have adverse effects. For example, consider an individual who received an employer ETP due to redundancy and elected to roll this into superannuation. If they did not find other employment for some time, they would be forced to use part of their savings. These people are likely to have difficulties in meeting daily expenses and supporting their family from their own resources if their only significant savings is their employer ETP locked up in the superannuation system.